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PUBLIC SERVICE COMMISSION

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF KENERGY CORPORATION FOR REVIEW AND APPROVAL OF EXISTING RATES	)))	CASE NO. 2003-00165

BRIEF OF THE ATTORNEY GENERAL

Upon direction from the Commission that Kenergy must follow up on the Commission's Order in Case No. 200-395,[1] Kenergy filed a general rate case in June 2003. Kenergy asked for review and approval of its existing rates on the grounds that fiscal circumstances do not warrant a rate raise or a rate reduction. The Attorney General ("AG") and the Kentucky Industrial Utility Customers, Inc. ("KIUC") intervened. Discovery followed.

KIUC, through its witness Russell Klepper, filed testimony seeking a reduction in the rates of those direct serve customers it represents of $496,874 and a change in the distribution fee charged to Weyhauser on self-generated energy.[2] The Office of the Attorney General, through its witness, David Brown Kinloch, filed rebuttal testimony supporting Kenergy's contention that a change of rates is not appropriate at this time and discussing why it would be inappropriate to grant the changes requested by KIUC.[3] Kenergy filed rebuttal testimony maintaining that KIUC's request for a rate reduction should not be granted, that the utility should remain revenue neutral if any reduction is granted, and that if reductions are to be granted,

[1] See, Orders dated June 29, 2001 and December 11, 2002, in The Application of Kenergy Corporation for a General Adjustment in Existing Rates (Rate Reduction), Case No. 2000-395.
[2] See, Direct Testimony of Russell L. Klepper filed on behalf of Kentucky Industrial Utility Customers, Inc.
[3] See, Rebutttal Testimony of David H. Brown Kinlock filed on behalf of the Office of the Attorney General, November 2003.

customers other than the KIUC direct serve customers should receive reductions first based on cost of service considerations.[4]

ARGUMENT

RATES SOULD REMAIN AS THEY ARE NOW. WEYHAUSER HAS CONTRACTED AWAY ITS RIGHT TO COMPLAIN.

Following the merger of Green River and Henderson Union to form Kenergy, the Commission granted Kenergy's request to implement a five year 4% decrease (estimated to be worth $2,289,780 per annum) in the rates of the non-direct serve customers via a consolidation credit rider to be in effect from September 2, 1999 to September 1, 2004.[5] In that same Order, the Commission reserved the question of the proper energy charge adder for direct serve customers for the next rate case. In the next general rate case, Case No. 2000-395, the Commission granted the KIUC direct serve customers a rate reduction of $252,000 (KIUC had sought a substantially larger rate reduction) that was implemented in conjunction with a change in the design of the rates charged to these direct serve customers. In granting the rate decrease for the KIUC direct serve customers, the Commission recognized that non-cost factors must be taken into account when setting rates.[6]

In this case, Kenergy argues that its rates should be neither raised nor lowered. It also argues that should there be any internal adjustment to the rates of any of the classes, it should be held revenue neutral. In this case, based on a cost of service analysis, KIUC argues that its direct serve customers are entitled to a further rate reduction of $469,320. Mr. Klepper's supporting cost of service analysis is skewed by its exclusion of both the cost of Purchased Power and

[4] See, Rebuttal Testimony of Dean Stanley on behalf of Kenergy Corp.

[5] See, Order of June 14, 1999, in The Application of Green River Electric Corporation and Henderson Union Electric Cooperative Corporation for Approval of Rate Decrease for Kenery Corp., Consolidation Successor, Case No. 99-162.

[6] See, Case No. 2000-395, Order of June 29, 2001, pp. 7, 8, 11.

Interest on Long Term Debt. It should not be used as the basis for an adjustment of rates.

Klepper's contention that it is unnecessary for KIUC direct serve customers to make any further contribution to Kenergy's margin because of the size of the patronage capital accounts sounds of retroactive ratemaking in which future rates are predicated upon and/or correct for profits earned by the company under past rates. The size of the patronage accounts is irrelevant to the ongoing need for all customers to contribute to Kenergy's margin.

The testimony of David Brown Kinloch points out the problems of attempting to utilize traditional cost of service methodology to determine appropriate cost allocation in the situation presented by Kenergy and its direct serve customers. Instead of using traditional cost of service methodology in this situation, it would be appropriate to use each class's contribution to Kenergy's total revenue as a means of allocating revenue related expenses and credits. Under this analysis, KIUC's direct serve customers are not paying unduly high rates and no rate reduction for Class A and B members is warranted.

Kenery continues to face the extraordinary risk posed by providing service to such large customers. That is a significant risk that cannot be quantified and one that requires the utility to maintain a strong financial position. In 2004, the RUS TIER requirement for Kenergy moves from 1.0 to 1.25. If a rate reduction is granted to KIUC members, it will have to be recovered from non-direct serve customers if Kenergy is to be held revenue neutral. Should that be done, non-direct serve customers will lose a part of the benefit for which they bargained in approving the merger.

In September 2004, the consolidation credit expires, resulting in a $2.5 million rate increase for non-direct serve customers. The KIUC customers will continue to enjoy the rate reduction gained in Case No. 2000-395 after the non-direct customers face the increase in rates posed by the expiration of the consolidation credit. The principles of revenue stability, rate continuity and gradualism will not be served by throwing a rate reduction of $469 plus thousand for five customers into this mix.

The financial position of Kenergy is such that had the Commission not demanded it, there would have been no reason for them to come in for a rate case. Because of this, the AG supports continuation of the current rates of Kenergy. A mid-stream rebalancing of the rates to be paid by the various classes of ratepayers absent any need by the utility for a change in its overall revenue requirements is unwarranted. This is particularly true here because the Commission, in Case No. 2000-395, has already examined the rates of the direct serve customers vis-à-vis the same overall revenue requirement for Kenergy that will continue once this case is complete.

The effort to reform the charge to Weyerhaeuser appears to be directly in contravention of the contract terms between Weyerhaeuser and Kenergy and should be denied.

Respectfully submitted

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NOTICE OF FILING AND CERTIFICATION OF SERVICE

I hereby give notice that I have filed the original and ten true copies of the foregoing with the Executive Director of the Kentucky Public Service Commission at 211 Sower Boulevard, Frankfort, Kentucky, 40601 this the 22nd day of December, 2003, and certify that this same day I have served the parties by mailing a true copy, postage prepaid, to the following:

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